NO. 16119

COURT OF APPEALS

for the Ninth Circuit

D. W. CLARK and UNION OIL COMPANY OF CALIFORNIA, a corporation,

Appellants,

vs.

MURRAY D. AGATE, TRUSTEE IN BANKRUPTCY of the Estates of ALTON C. SIMMONS, CECELIA MAE SIMMONS, ALVIN L. SIMMONS, ODA JANE SIMMONS and LAWRENCE W. SIMMONS, individually and as co-partners, DBA ALPINE LODGE,

Appellees.

BRIEF FOR APPELLANTS

Appeal from the United States District Court for the District of Oregon.

HONORABLE WILLIAM G. EAST, Judge.

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JURISDICTION

This is a limited appealed from an amended judgment entered by the United States District Court for the District of Oregon, sitting as a court of bankruptcy, for the recovery by a trustee in bankruptcy of a voidable preference.

Jurisdiction of the cause stems from Bankruptcy Act, § 1(10) and § 2 (11 USC § 1(10), § 11) for the District Court and from Bankruptcy Act, § 24 (11 USC § 47) for the United States Court of Appeals.

The Pre-Trial Order below (R. 8-16), which superseded the pleadings of the parties, shows the existence of the jurisdictions.

STATEMENT OF THE CASE

During the times pertinent to this cause, five persons named Simmons were co-partners, doing business as Alpine Lodge, a general partnership (R. 17). There were no other partners (R. 20).

In May 1954, the co-partnership effected four transfers, which were the subject of the purported voidable preferences. These were:

1. To D. W. Clark, May 3, 1954, an account receivable from C. E. Grooms, worth $229.91.
2. To D. W. Clark, May 3, 1954, an account receivable from Oregon Film Service, worth $422.24.
3. To D. W. Clark, May 20, 1954, the sum of $228.85.
4. To Union Oil Company of California, May 20, 1954, the sum of $2271.15 (R. 17, 18).

For purposes of this appeal only, appellants will assume the truth of certain findings of fact entered by the Court below (R. 17, 18, 19) the gist of which is that the transfers had the characteristics of voidable preferences, that each transfer was on account of an antecedent debt,

that the partnership was insolvent when each transfer was made, that the effect of the transfers was to enable the transferees to obtain greater percentages of their debts than other creditors of the same class, and that the transferees had reasonable cause to believe that the transferring partnership was insolvent when the transfers were made. These questions were litigated and decided adversely to appellants. Although not acquiescing in the truth of the findings, appellants do not wish to re-litigate those issues.

Later, two partners as individuals filed voluntary petitions in bankruptcy and were adjudicated bankrupts on the date of filing, August 9, 1954. The next day the remaining three partners as individuals filed voluntary petitions, and each was adjudicated bankrupt on that day (R. 19-20).

No petition or other document whose purpose was to bring firm assets under the Court's jurisdiction was filed by or against the partnership until the following spring. On March 25, 1955 the trustee of the individual Simmons' estates in bankruptcy filed a purported petition for adjudication that the partnership was bankrupt, referring therein to Bankruptcy Act, § 5i (11 USC § 23i). On March 31, 1955, came the actual adjudication that the partnership was bankrupt (R. 20).

Still later, on April 12, 1955, all the partners submitted a voluntary petition for the partnership's adjudication in bankruptcy (Ex. 5).

In 1956 the trustee of all the partners' estates and of the partnership (R. 17) sought under Bankruptcy

Act, § 60 (11 USC § 96) to recover the four transfers described above as voidable preferences. The issues and contentions were defined in Judge William G. East's Pre-Trial Order of December 18, 1956 (R. 8-16). The pre-trial conference was held upon October 29, 1956 (R. 8). One issue there discussed, and the only issue in this appeal, was this: Did the four transfers occur within the time period during which transfers may be voidable preferences as defined in Bankruptcy Act, § 60a(1) (11 USC § 96a (1)). (R. 13-14)

Addressing himself to this issue, Judge William G. East authored a Memorandum Opinion dated November 20, 1956 (R. 1-6). The issue is framed by this language taken therefrom:

> "Counsel has stated the question involved under the foregoing agreed facts as being whether the alleged perference occurred within four months before the filing of the petition in bankruptcy of the transferor, bankrupt, Alpine Lodge, a co-partnership, as required by Sec. 60 of the Bankruptcy Act, Title 11, U.S.C.A. Sec. 96.
>
> "It is apparent from the agreed facts that more than four months did expire between the date of the alleged preference and the filing of a petition in bankruptcy by the mentioned co-partnership. The legal question presented is better stated as whether or not the alleged preference occurred within four months before the co-partnership was in fact and in law adjudged a bankrupt.
>
> * * * * *
>
> " . . . it appearing conclusively that four months had not elapsed after the date of the alleged preference and before the adjudication of all the copartners as bankrupts, therefore, the question is answered in the affirmative that the alleged prefer-

ence was made within four months before the adjudication of the co-partnership as a bankrupt."

In his findings of fact and conclusions of law entered April 23, 1958, Judge East continued in his persuasion that the time-limit requirement of Bankruptcy Act, § 60a(1) (11 USC § 96a(1)) was satisfied (R. 23, Conclusion of Law 4). The transfers were held to be voidable preferences.

The transferees, appellants, for purposes of the appeal, seek only a review of the bankruptcy court's determination of that single question, whether the transfers fell within the prescribed four-months' period.

SPECIFICATION OF ERRORS

The bankruptcy court erred in concluding in its memorandum opinion of November 28, 1956, and specifically in the last paragraph thereof (R. 5-6), and in its Order of December 5, 1955 (R. 6-8), and in its Findings of Fact and Conclusions of Law of April 23, 1958, and specifically in Conclusion of Law No. 4 (R. 23) that the four purported preferential transfers were effected within the four-months' period specified by Bankruptcy Act, § 60a(1) (11 USC § 96a(1)).

SUMMARY OF ARGUMENT

The four transfers germane to this matter were partnership, not individual transfers. Bankruptcy Act, § 60a(1) (11 USC § 96a(1)) renders voidable certain transfers made within the fourth months next prior to

the filing of a petition by or against the transferor. Nothing was filed by or against the transferor until March 25, 1955 or April 12, 1955, either of which dates fall well without the four months' period.

ARGUMENT

A. Preferences effected more than four months before the filing by or against the transferor of a petition in bankruptcy are not voidable.

Part of the definition of a preference, set out in Bankruptcy Art, § 60a(1) (11 USC § 96a(1)) is:

> " . . . a transfer . . . by such debtor . . . within four months before the filing *by or against him* of the petition initiating a proceeding under this Act. . . ." (Emphasis supplied)

This fourth month period is computed from the filing of the transferor's petition, not some other petition. For instance, in a case arising from Puerto Rico, *Credito y Ahorro Ponceno v. Gorbia,* 25 F2d 817 (1st Cir., 1928), cert. denied 278 US 613, 49 S Ct 18, 73 L ed 537, the converse of the case at bar was considered. There, during the course of an exceedingly complex property security transaction between a partnership and a financing bank, the partners made individual transfers to the bank of their individual property. In bankruptcy proceedings commenced by a petition against the firm only, the District Court held these transfers to be voidable preferences. This was reversed upon appeal. Partners' individual transfers are not preferential in the partnership's bankruptcy, even though to a firm creditor. The rationale of the case is that the transferors-in-fact did

not constitute the debtor-bankrupt-transferor contemplated by Bankruptcy Act, § 60a(1). An esteemed state court concluded the same in *Tate v. Hoover,* 345 Pa 19, 26 A2d 665 (1942), cert. denied 317 US 677, 63 S Ct 159, 89 L ed 543.

In addition, states III Collier on Bankruptcy (14th Ed) 790, § 60.10:

> "And the trustee of a bankrupt member of a partnership may not recover firm assets which have been transferred preferentially, the right to recover in such a case inures to the benefit of the firm (citing *Rubenstein v. Lottow,* 220 Mass 156, 107 NE 718, 16 ABR 243)."

In the case at bar, there were partnership transfers of partnership assets (R. 9, 17-18) within four months prior to the individual petitions but more than four months prior to the trustee's petition for partnership adjudication of March 25, 1955, or the partnership petition filed April 12, 1955, whichever of these two be the "petition" under Bankruptcy Act, § 60a(1).

The four month rule is inexorable. The opinion in *Gates v. First National Bank of Richmond,* 1 F2d 820 (D.C.E.D. Va, 1924), in reciting the elements of a voidable preference, commences with (1 F2d at 822):

> "First, there must have been a payment within four months of bankruptcy [N.B. 'Bankruptcy' with reference to time, means the date the petition was filed. Bankruptcy Act, § 1(13) (11 USC § 1(13))]; this is the line of demarcation. It does not make any difference how insolvent a man may have been, or how clearly the intention to create a preference, it must have been within four months."

Closely analogous to Bankruptcy Act, § 60, is § 67, which relates to setting aside liens obtained within four months next prior to filing of the petition. The Fifth Circuit, in *In re Louisell Lumber Co.,* 209 Fed 784 (1913), properly detected the dual purpose of the four month limitation. To be sure, that period is established so that the trustee can undo that which was done by the bankrupt; but also:

> "The limitation of four months protects and preserves liens so obtained four months before the filing of the petition." 209 Fed at 786.

It is this policy favoring the stability of transactions which lie without the prescribed four months' period which appellants seek to invoke.

B. A partnership and its individual constituent partners are separate entities under the scheme of the Bankruptcy Act.

Bankruptcy Act, § 5 (11 USC § 23) is the principal statutory matter on partnerships in bankruptcy.

I Collier on Bankruptcy (14th Ed) 691-692, after describing the partnership as an entity distinct from the partners, continues to describe the principal consequence:

> "As such legal entity, a partnership owns its property, and owes its debts, apart from the individual property of the members which it does not own and apart from the individual debts of its members which it does not owe."

and continues on page 693:

> "Although the Act of 1938 attempts to integrate more carefully the machinery for adjudication of the partners, and of the firm, and to resolve vari-

> ous difficulties which arose under the Act of 1898, the entity theory has been retained as the keynote of § 5."

Although the Uniform Partnership Act is considered to reflect the aggregate rather than entity theory of partnership as a business form, the separate quality of partnership property is deeply embedded in certain of its sections. For instance, Oregon Revised Statutes 68.130(1) defines partnership property:

> "All property originally brought into the partnership stock or subsequently acquired by purchase or otherwise, on account of the partnership is partnership property."

And ORS 68.420 establishes the peculiar incidents of specific partnership property:

> "NATURE OF A PARTNER'S RIGHT IN SPECIFIC PARTNERSHIP PROPERTY. (1) A partner is co-owner with his partners of specific partnership property, holding as a tenant in partnership.
>
> "(2) The incidents of this tenancy are such that:
>
> "(a) A partner, subject to the provisions of this chapter and to any agreement between the partners, has an equal right with his partners to possess specific partnership property for partnership purposes; but he has no right to possess such property for any other purpose without the consent of his partners.
>
> "(b) A partner's right in specific partnership property is not assignable except in connection with the assignment of the rights of all the partners in the same property.
>
> "(c) A partner's right in specific partnership property is not subject to attachment or execution, except on a claim against the partnership. When partnership property is attached for a partnership

debt the partners, or any of them or the representatives of a deceased partner, cannot claim any right under the homestead or exemption laws.

"(d) On the death of a partner his right in specific partnership property vests in the surviving partner or partners, except where the deceased was the last surviving partner, when his right in such property vests in his legal representative. Such surviving partner or partners, or the legal representative of the last surviving partner, has no right to possess the partnership property for any but a partnership purpose.

"(e) A partner's right in specific partnership property is not subject to dower, curtesy, or allowances to widows, heirs, or next of kin."

A tenancy in partnership is a statutory creation. Assume that a law partnership possesses an extensive library, held in such tenancy. Under the statute just set forth, any partner may possess and use the books for the business of the firm; but he cannot, except in conjunction with his follow-partners, assign his rights in the books to the lawyer across the hall. Nor can the groceryman or other individual creditor of a partner attach or execute upon the partner's interest in the books or the books themselves.

The alleged preferential transfers in the case at bar were partnership transfers of partnership property (R. 9, 17-18). Because of ORS 68.420, this partnership property was not available in satisfaction of individual debts by attachment or levy. Therefore, this property is akin to a corporate asset.

Appellant concedes that the entity theory's being incorporated into the Bankruptcy Act, and into the

property sections of the Oregon version of the Uniform Partnership Law, does not in itself solve the problem on appeal. But any encroachments upon the entity theory should be considered as specific aberrations and appropriately defined in scope.

One aberration is that described in the selection from Collier, *supra,* as an attempt to integrate better the adjudication of a partnership and members of the partnership as bankrupts. This is the first sentence of Bankruptcy Act, § 5i (11 USC § 23i):

> "i. Where all the general partners are adjudged bankrupt, the partnership shall also be adjudged bankrupt. In the event of one or more but not all of the general partners of a partnership being adjudged bankrupt, the partnership property shall not be administered in bankruptcy, unless by consent of the general partner or partners not adjudged bankrupt; but such general partner or partners not adjudged bankrupt shall settle the partnership business as expeditiously as its nature will permit and account for the interest of the general partner or partners adjudged bankrupt."

There is nothing in this which eradicates the requirement of Bankruptcy Act, § 60a(1) that the computing of the four months' period commences with the petition of the transferor, in the case at bar, the partnership.

C. Automatic adjudication of a partnership as bankrupt does not affect the substantive requirements of Bankruptcy Act, § 60a(1) (11 USC § 96a(1)).

The Court below has concluded, based upon certain text from Collier on Bankruptcy, that, when all general partners are individually adjudicated, the partnership is

automatically adjudicated bankrupt without any further petition (R. 5).

Whether or not Bankruptcy Act, § 5i allows a partnership adjudication upon the Court's own motion under appropriate circumstances, in the case at bar, there was a partnership petition in fact. The Court never did adjudicate the partnership on its own motion. Appellants submit that the District Court's conclusion that the four months is computed from the time when the partnership "was in fact and in law adjudged a bankrupt" (R. 4) is a somewhat too violent construction of Bankruptcy Act, § 60a(1). That section has nothing to do with the date of adjudication. Where there is actually filed a partnership petition, the obvious answer to the question on appeal is that the date of its filing is the very date described in § 60a(1).

This Court, therefore, need not decide what happens when there is no partnership petition and all partners are adjudged bankrupt, for that is a more complex case not now presented. This is an appropriate case for the selection of the simple solution.

In the instant case, Bankruptcy Act, § 5i does no more than provide for a judicial declaration of the partnership status. There is nothing operative in that section relative to the various bankruptcy remedies. Bankruptcy Act, § 1(2) (11 USC § 1(2)) defines:

> " 'Adjudication' shall mean a decree that a person is bankrupt; . . ."

In *First National Bank of Goodland v. Pothuisje et al,* 217 Ind 1, 25 NE 2d 436, 130 ALR 1238 (1940),

the Court described an adjudication in bankruptcy:

> "An adjudication in bankruptcy is a judgment in rem as to the assets brought into the court and establishes the status of the debtor. It absolves the bankrupt from no agreement, terminates no contract, and discharges no liability." 130 ALR at 1240.

Nor does adjudication sweep into the bankrupt estate transfers by the debtor, even though they may be preferential. There must still be compliance with § 60a(1). The four months must still be computed from the date of the transferor's petition.

> "The whole statute must be considered and all of its parts given their obviously intended meaning and purpose. No part should be stricken down unless it be in irreconcilable conflict with the remainder." (*Fetzer v. Johnson,* 15 F2d 145, 151 (C.C.A. Okla, 1926), cert denied 273 US 751, 47 S Ct 455, 71 L ed 873.)

It should be recalled that at common law, preferences were not considered evil. The Bankruptcy Act, like death, is the great leveler, at least for the diligent creditor. But the Act cannot be permitted to level that which lies beyond its four months' limitation.

For instance, in *In re Hall,* 27 F2d 999 (D.C.W.D. Pa, 1928), one Hill, creditor of Hall, filed an involuntary petition, alleging that Hall's creditors numbered less than twelve. The referee discovered eighteen creditors, but initially excluded three relatives and one fully secured creditor from the counting list pursuant to the Act. That left fourteen. Next the zealous referee excluded three more creditors: An $8.00 room rent creditor, a $5.00 cigar creditor, and a $20.00 board creditor. The ref-

eree justified these latter exclusions by concluding that the spirit of the Act did not allow the inclusion among the twelve counting creditors of persons with small current accounts. He was reversed, as the District Court dismissed the petition, following the Act as it prescribes that one creditor can file an involuntary petition only when the total is less than twelve. The opinion, at page 1000, states:

> "In view of the facts developed, we have been somewhat reluctant in arriving at our conclusion that the petition must be dismissed. The dismissal seems to us to be in direct opposition to the spirit of the Bankruptcy Act, which seeks an equitable distribution of an insolvent's estate among his creditors. To sustain the exceptions to the referee's report means that the entire estate will be taken by two creditors—one of them the mother of the debtor—to the exclusion of other creditors of equal degree. . . . However, it is not our duty to allow the direct letter of the Bankruptcy Act to be overthrown by our conception of the spirit of that Act. . . ."

In the instant case, the direct letter of the Act is entirely supportive of appellants' position. Nor is the spirit violated by upholding a transfer as being too remote from the date of filing.

CONCLUSION

Appellants urge to this Court that Bankruptcy Act, § 60a(1) is a statute whose application is essentially mechanical, and that the mechanics of that section require a conclusion that the purported preferential transfers in issue occurred prior to the period established by the Act.

Respectfully submitted,

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